

The Financial Benefits of Merger of Further Education Colleges

**THE
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COUNCIL**

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The purpose of the FEFC is to secure further education provision which meets the needs and demands of individuals, employers and the requirements of government in respect of the location, nature and quality of provision.

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Preface

Often, when Council staff meet with college staff or governors, they are asked, ‘what are the financial benefits of merger?’. It is only recently, with over 20 mergers having been agreed and with some of those mergers now well-established, that robust data have become available. The Council therefore commissioned KPMG to undertake a limited study.

The study was intended to act as a guide. It is not a manual, and the benefits identified will not all be possible in every merger. The study provides the views of those colleges which have been involved in merger, who were asked to describe financial benefits which could not have been achieved at all, or as easily, without merger.

Whilst the study primarily relates to the financial benefits of merger, it is helpful that colleges have stressed the associated costs and, most significantly, that colleges consider, in general, that curriculum benefits outweigh the financial.

The Council thanks those colleges which so willingly gave of their time to assist in the study.

We hope that the experience of others will assist college managers and governors to ensure that future mergers achieve the maximum benefits available, whilst avoiding any pitfalls.

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1 Introduction

Background

1.1 Since the creation of the further education (FE) sector in 1993, there have been 29 mergers of FE institutions which have taken place in England out of a total of 464 institutions. These mergers have been of several different types including:

- merger of a general FE college and a sixth form college
- merger of two general FE colleges
- merger of two sixth form colleges
- merger of specialist colleges and general FE colleges
- mergers of two specialist colleges.

There have also been mergers of FE and HE institutions, although these have not formed part of this study.

1.2 The actual merger mechanisms employed have been of two types:

- type A – in this situation, all the existing corporations are dissolved and a new corporation is formed to take their place. The new corporation, which may and probably will adopt a different name from either of the two original corporations, takes over the assets and liabilities of the old corporations
- type B – in this situation, all but one of the existing corporations are dissolved and the remaining corporation takes over all of their assets and liabilities. The name of the remaining corporation may also be changed to reflect the nature of the merged institution.

1.3 In November 1997 the secretary of state for education and employment wrote to the chair of the Further Education Funding Council (FEFC) that:

... I also want to see a more proactive approach to mergers so that the sector will be better placed to live within what will always be limited resources.

This statement indicates clearly the policy of the government in this area. As part of its response the FEFC commissioned an independent study of the financial benefits which have resulted from the merger of colleges in the FE sector which have already taken place. KPMG were commissioned to carry out the research which was undertaken in March and April 1998. This report provides the findings of that study.

Aims

1.4 The overall aim of this report is to provide guidance for college governors and principals who are contemplating merger with another college and who might wish to know something of the experience of other colleges which have undertaken merger since the establishment of the further education sector.

1.5 The specific aims of the study were to:

- identify the underlying objectives and ambitions which led to those institutional mergers which have already taken place
- identify the financial and other benefits which merger has produced or is anticipated to produce, and to consider whether such benefits could have been realised by other means
- identify the costs, both financial and human, which have had to be incurred to achieve merger
- identify factors which colleges contemplating merger should take into account when choosing a merger partner and in evaluating a merger option
- evaluate the processes of planning and implementing a merger, to point out areas of good practice and to warn against possible pitfalls.

Approach

1.6 Ten colleges in England were selected for study in this review. The selection included general further education colleges, specialist colleges and sixth form colleges. Different combinations and types of merger were examined within and between these groups. Geographic spread was also used as a selection criteria. It was also recognised that, as all the mergers involved had taken place since 1993 (and some since 1996), some medium- and long-term benefits had yet to be achieved. In seeking to reach general conclusions, the authors recognise that each merger is to some extent unique, as a result of background, local context and identified needs. However, a number of common factors have been identified, and a pattern of 'good practice' is beginning to emerge in the light of experience. This the authors consider valuable in supporting colleges considering or about to embark upon the merger process.

1.7 Before the fieldwork visits, the colleges selected for the study were briefed on the purpose of the study and asked to make available certain key financial information describing their 'pre-merger' position, along with their financial forecasts. Equivalent information was also requested for the first post-merger period and subsequently, for comparison. Similarly, other 'pre-' and 'post-' merger strategic planning information was requested including the 'option evaluation' undertaken by each merger partner, and the joint merger submission documentation. Where possible, each merged institution provided an analysis of the main financial benefits and costs associated with the merger to date.

1.8 At the fieldwork stage, nine of the colleges selected for the study were visited. Interviews were conducted with senior and middle academic and support managers and, where possible, with governors who had been particularly involved before and throughout the merger and post-merger periods.

1.9 The information obtained both from the documentation and from the fieldwork visits was then pooled and analysed in order to identify significant circumstances, recurring issues, critical success factors and good practice. Firm quantitative information was not always available and so judgements sometimes had to be made. Throughout this report we have attempted to assess whether particular financial benefits deriving from merger were significant, moderate, minimal or non-existent. In making these judgements about the significance of financial benefits we are not referring to absolute amounts but to the scale of the benefit compared with the scale of the institution involved.

General Findings

1.10 Before looking in some depth at the findings of the study it is worth setting out some general findings. These are given below:

Merger purpose

1.11 In most cases, the prime consideration which had led to merger was not the achievement of cost-savings but the preservation and sustenance of a wide range of high-quality provision in a locality where it was perceived that some areas of provision might be 'at risk' in the medium- or long-term.

Structure of merger

1.12 All of the mergers studied during the course of this review can be regarded as being broadly successful, in terms of achieving the objectives originally set. However, with the benefit of hindsight, some college acknowledged that other options might have been pursued. Often these options would have involved three rather than two institutions. Consequently, a thorough appraisal of merger options is a prerequisite for merger, and further mergers among those institutions which have already merged cannot be ruled out.

Benefits realised

1.13 There was clear evidence that there had been substantial benefits derived from merger. Some of the benefits were related to improvements in the quality and range of curriculum offered; others were financial and involved additional income and/or cost savings. The nature of these benefits will be outlined in the remainder of this report.

Timescales

1.14 The earliest mergers reviewed during the course of this study had taken place in 1994; others had taken place in 1997. Consequently there was a clear view that only part of the benefits of merger had been realised and further benefits were anticipated in the years ahead.

Merger impact

1.15 It appears to the authors that the financial benefits identified in this report could not have been realised in the absence of merger. Although it could be argued that, in theory, some of the benefits could have been achieved by other means, in practice it seems unlikely that this would have occurred for a variety of reasons. Certain other benefits were, by definition, achieved as a result of merger.

Transferability of benefits

1.16 No generalisations can be made about the benefits and costs of merger. In the body of this report some of the achievements that have been made through merger are described but it is clear that these achievements are specific to the particular merger concerned. It must be emphasised therefore that before embarking on merger it is vital that the specific merger proposal is fully evaluated to identify the prospective costs and benefits involved. Colleges should not assume that the benefits and costs which have applied in other merger situations will necessarily apply in all cases.

Merger process

1.17 The work associated with the achievement of merger should never be underestimated. The merger process involves extensive commitment of senior staff time, and must be organised to ensure that the service to existing customers and clients does not suffer during the process.

■ 2 *Context and Objectives*

Introduction

2.1 Before considering the actual and prospective benefits of merger achieved by the nine institutions reviewed, it is important to describe, first, the context in which merger was planned and implemented and the objectives conceived at the time of their consideration.

Context

2.2 Although some mergers of FE institutions took place before 1992 the mergers reviewed in this study have all taken place since then. During that period the FE sector faced a number of challenges and thus the contextual background of merger is complex. The following factors are considered to have been the most influential of these.

Prior collaboration

2.3 A common feature across the sample of colleges included in the study was that there had been a history of some collaboration between the merger partners, and consideration of merger proposals at various times, dating back to pre-1992. This had led, in two cases, to mergers taking place shortly after 1992.

Competitive environment

2.4 For the majority of institutions, the post-incorporation requirements for more extensive market needs analysis, strategic planning and financial forecasting at institutional level had enabled the colleges concerned to form a more accurate picture of their own and relative positions and of the strategic options available to them. The increasingly competitive climate, the efficiency gains required of the sector in the first post-incorporation period, and the 'benchmarking' information available to corporations and senior management, all served to raise institutions' awareness of the likelihood of future success, development and indeed survival. Smaller and more specialist institutions including sixth form colleges had felt that their future options were limited and that their provision was particularly at risk, despite their being the sole provider of some curriculum areas in their locality.

Senior staff and board member changes

2.5 Sometimes the departure of a chief executive had prompted college boards to explore the merger option before advertising for a replacement. In some cases the appointment of one or more new chief executives or senior governors in a locality provided a different climate for dialogue between erstwhile 'competitors'.

Forward thinking and collaboration

2.6 Several colleges mentioned that they had felt they would prefer to 'steer' their colleges into appropriate merger arrangements from a relatively strong negotiating position rather than wait until forced to do so as a result of a deteriorating financial profile and the consequences of wasteful competition with neighbouring colleges for relatively static markets.

2.7 In some cases, collaborative arrangements, including joint bidding for additional resources, joint student admissions systems, staff development activities, purchasing of external services from contractors, purchasing of materials and equipment and even joint staff appointments had already been established. As a result, the institutions involved had become familiar with each other's personnel and procedures. Full merger was considered the next logical step to these arrangements in order to achieve greater benefits and further efficiency gains.

Rejection of merger options

2.8 A number of alternative options had been explored in most cases before merger, although not always in great depth, and had been rejected. Reasons for rejection had included:

- incompatible missions and aims or a culture clash
- fear of asset-stripping, loss of identity and influence
- exacerbation rather than alleviation of financial problems
- requirement for extensive rationalisation, in the short-term, and areas of work being placed 'at risk'
- significant risks to recruitment as a result of 'change of image'
- inability to agree governance and organisational structure of the proposed institution
- inability to achieve significant benefits through limiting factors outside the control of either merger partner.

2.9 In this last respect, several colleges stated that a more 'complete solution' for a locality would have been the merger of all the FE providers at the same time, in order to eliminate competition and gain the maximum efficiency savings. However, in the absence of a commitment to such a proposal by one or some of the local providers, they felt that they had at least placed the merged institution in a strong position in future negotiations on this issue.

Objectives

2.10 A number of objectives have been identified which were foremost in the consideration of those colleges considering merger. These are outlined below.

Curriculum benefits

2.11 For all colleges in the sample, the overriding aim of the merger was the preservation and ongoing support of the curriculum areas in which they were involved, particularly those deemed to be at risk or 'minority' areas. It was felt that the economies of scale of a larger institution would offer protection to these areas of provision and that efficiency of delivery would be enhanced, as it was likely that group sizes would increase, thus sustaining financial viability. It was also thought that wider curriculum choice and access and better learning support facilities would encourage students to enrol with the merged college rather than at another college in the locality. However, some of the smaller colleges were concerned that the risk to their identity and hitherto perceived 'friendly, caring, quality image' might discourage applicants to the merged college. They had therefore agreed to launch an extensive marketing campaign to overcome this potential risk in the run up to and at the point of merger.

Defensive reaction

2.12 At least half of the colleges in the sample identified their merger as partly defensive; that is to say, it was done to avoid the possibility of the partner college merging with another potential competitor.

Greater presence

2.13 Most of the colleges interviewed perceived the merger as having given them a greater sphere of influence and greater presence at the negotiating table with external stakeholders and potential partners, such as the training and enterprise council (TEC), higher education (HE) providers and local industry and commerce. They also felt that the reduced number of FE managers attending such meetings provided a greater coherence of views and represented a significant saving in terms of management time.

Space utilisation

2.14 Some colleges had aimed, through merger, to increase the space available for development and also to improve the quality and utilisation of their existing accommodation. Of all the aims included in their merger proposals, this one had been most consistently fulfilled and exceeded. Investment and/or reinvestment of capital released as a result of merger in new accommodation and in improving the quality of existing accommodation had already taken place or was planned in the near future in most colleges in the sample. Moreover, the aim of improving the asset base of the institution had been accomplished, and colleges now felt more confident in obtaining improvement and development loans in order to support their accommodation strategies.

Administrative efficiencies

2.15 The aim of improving the efficiency of college systems has been achieved largely through sharing good practice and pooling expertise. For smaller colleges, the lifting of a number of administrative burdens from staff who were previously performing several key functions has improved efficiency.

Timescales

2.16 In some cases, colleges had been optimistic in terms of the timescales envisaged for realising the benefits. Generally, it took two or three years before the benefits of joint curriculum development or structural reorganisation were achieved. The time taken for systems harmonisation had sometimes been under-estimated, as had the time required by senior management to bring about effective communications systems and the adoption of consistent practice across all college sites. Aims concerning the practicalities of the two merger partners operating as a single merged institution were sometimes missing from submission and consultation documents, and not reflected in the merged institution's financial forecasts in the first post-merger period.

■ 3 *Benefits*

Introduction

3.1 This chapter considers the benefits that are achievable from the merger of two or more FE colleges. As we have already emphasised, the key driver in all of the mergers we have studied during this review was the ability of the merger to generate improvements in the range and quality of curriculum of the merged institution. This is an issue to which we will return, but initially we consider the range of financial benefits which merger has produced. The various benefits identified are discussed under the following headings:

- site rationalisation
- support service savings
- academic cost savings
- income generation
- curriculum benefits
- organisational benefits.

Site Rationalisation

3.2 Merger of two or more institutions can lead to a situation in which it is feasible to reduce the volume and range of physical estate needed by the merged institution without having serious negative effects on service provision. This can generate two main financial benefits; in running costs and sale proceeds.

Running costs

3.3 Merger can enable a reduction in buildings running costs such as maintenance, cleaning, administrative support and communications. However, such savings are, generally, only significant where the buildings are being closed completely. The nature of some of the costs involved means that a partial closure often only results in a relatively small reduction in cost being generated (for example, heating) whereas the complete closure of a building will enable those costs to be reduced to zero.

Sale proceeds

3.4 These are the proceeds from the eventual sale of the land and/or buildings which have been closed. Clearly the value of the proceeds will depend on a number of factors such as size, condition, potential development status and so on.

3.5 The nine colleges in our study have identified both actual and potential capability for site rationalisation as shown in table 1.

Table 1. Financial benefits of site rationalisation

	<i>Significant</i>	<i>Moderate</i>	<i>Minimal</i>	<i>None</i>
Savings in running costs achieved	1	2	2	4
Future savings in running costs expected	4	1	4	—
Proceeds from the disposal of land and/or property achieved	1	—	2	6
Future proceeds from the disposal of land and/or property expected	6	—	2	1

Sample: nine colleges

3.6 Many of the colleges in the study have, as yet, made little major change to their use of accommodation for the purpose of achieving cost-savings although there has been some relocation of provision for curriculum reasons. However, most do anticipate making such change over the next few years.

3.7 The following examples illustrate the sorts of benefits which have been achieved and which are anticipated.

3.8 One merged college, originally on three sites, has already closed an inner city site and relocated its services at a larger and more suitable site a few miles away. This has already resulted in savings in running costs of some £50,000 a year. However, it is anticipated that the net sale proceeds from the site will be minimal due to its condition and location.

3.9 Another merged college is based on two main sites, one of which is a large rambling site, economically inefficient to operate and unsuitable for learning purposes. The college is considering taking out a lease for new accommodation in the city centre which will provide better, cheaper and more suitable accommodation for the course provision it plans to offer. The existing site can then be largely disposed of and, since it is located in a prime residential area, the sale proceeds of the land could be as much as £2 million to £3 million.

3.10 A third merged college had already disposed of one site as a consequence of merger. The savings in running costs (£310,000) exceeded the costs of disposal (£265,000) in the first year. In addition the ultimate disposal of the site generated further proceeds.

3.11 It must be emphasised that the view of the colleges and ourselves is that the actual and prospective financial benefits from site rationalisation identified in the course of our study could not have been achieved without merger. It required the combination of two existing estates portfolios in order to identify certain estates provision which became surplus to the needs of the merged institution.

Support Service Savings

3.12 Under the heading of support services we have included a range of functions such as:

- senior management
- finance
- personnel
- estates management
- student support
- information systems/technology
- staff development
- marketing
- communications
- subscriptions, licences
- transport.

3.13 Support service savings in the sample of colleges are shown in table 2.

Table 2. Support service savings

	<i>Significant</i>	<i>Moderate</i>	<i>Minimal</i>	<i>None</i>
Level of savings generated	2	2	4	1
Future level of savings expected	—	3	6	—

Sample: nine colleges

3.14 Table 2 indicates that institutional mergers have not generated a great deal of savings, nor are likely to generate such savings, with regard to support services. This may seem somewhat surprising since the rationale for organisational merger both within the education sector and outside the sector is often thought to be the achievement of support service or administration cost savings. Paragraphs 3.15 to 3.20 provide reasons why support service savings may not have been generated.

Small institutions

3.15 In those situations in which a small institution is merged with a larger institution, the reality is that the smaller institution has, in cash terms, limited support service costs to begin with. For example, some small colleges have a chief administrative officer who combines the posts of finance director, personnel director and marketing director, which are separate posts in larger colleges. Merger of such an institution may only produce limited savings. Of the mergers studied during the course of this review, the majority fell into this category and thus, perhaps, give a false picture of the potential savings in this area achievable through merger.

Increased responsibilities

3.16 Savings in senior management posts (for example, one principal instead of two) are sometimes partly offset by an increase in remuneration costs of postholders in the merged institution, as a consequence of increased responsibilities.

Multi-site cost structure

3.17 By definition, all of the merged colleges were multi-site institutions at the time of merger. Multi-site occupation implies a higher cost structure than the equivalent single-site occupation because of the need to duplicate support services such as reception, transport, catering, student support and so on. Although, as discussed earlier, some limited site rationalisation has already taken place, most site rationalisation will take place in the future. Thus major support savings will probably be realised only when such rationalisation takes place.

Vacant posts

3.18 Once it is clear that merger is being contemplated it is common practice to keep many support service posts vacant, or even to delete the post, pending the merger. This reduces the support cost savings realised on merger.

Under-managed institutions

3.19 Some colleges claimed that before merger they were under-managed and that merger was used to strengthen their management arrangements and resources. Such actions, whatever their merits, mitigate against savings.

Contract arrangements

3.20 Many institutions reported that following merger, savings in the order of £30,000 to £80,000 a year were obtained by reducing contract arrangements for support services such as payroll or marketing. This was because the larger institution could often absorb the workload of the smaller institution at marginal cost, thus allowing the contract arrangement to be discontinued.

Academic Cost Savings

3.21 Table 3 shows academic cost savings in the sample of nine colleges.

Table 3. Academic cost savings

	<i>Significant</i>	<i>Moderate</i>	<i>Minimal</i>	<i>None</i>
Level of savings already generated	3	3	2	1
Level of savings expected to be achieved in the future	3	4	2	—

Sample: nine colleges

Academic management costs

3.22 This involves posts concerned with academic management such as heads of departments. Following merger, most colleges found it necessary to restructure their academic management arrangements to meet the needs of the merged institution. They often reduced the number of academic management posts by a fairly small number (typically three to five posts) although even this will have generated recurring savings of the order of £100,000 to £150,000 a year. However, a number of additional comments also need to be made about savings of this kind:

- sometimes such savings were achieved in advance of merger since certain vacant posts were not filled in anticipation of merger

- there were also costs involved which needed to be set against the cost-savings. (see chapter 4)
- in some cases, although certain academic management posts may have been rationalised, the postholder often remained in the institution on a protected salary.

Teaching staff costs

3.23 The savings in full-time teaching posts following merger has been minimal in all the colleges reviewed. In several colleges, teaching staff numbers had been substantially reduced as part of an earlier restructuring exercise, or posts had been left vacant in anticipation of merger. Colleges reported that following merger, rather than reduce staff numbers they undertook two main actions:

- existing full-time staff were more fully utilised to deal with the growth in student numbers
- expenditure on part-time teaching staff was, in some cases, substantially reduced.

3.24 There was a clear indication that, in order to provide for a smooth merger and to maintain staff morale, some colleges had not addressed the issue of teaching staff costs as robustly as they might. Such colleges believed that in the years ahead merger would put them in a position where they would be able to achieve considerable reductions in teaching staff through natural wastage with consequent staff savings. Such savings would not have been achievable without merger.

Teaching resources

3.25 In some cases, merger had placed an institution in a situation in which reducing duplication of the provision of specialist teaching equipment resulted in an immediate saving since a particular item was not replaced. In other situations, replacement policies could be amended with the result that forecast expenditure was lower than might have been the case without merger.

Income Generation

3.26 The additional income generated by colleges as a consequence of merger is summarised in table 4.

Table 4. Income generation in merged colleges

	<i>Significant</i>	<i>Moderate</i>	<i>Minimal</i>	<i>None /reduction</i>
Growth in FEFC income achieved	1	4	3	1
Growth in external income achieved	1	—	2	6
Growth in FEFC income anticipated	—	1	1	7
Future level of income growth anticipated				
FEFC	—	2	7	—
Other	—	2	6	1
HEFCE	1	2	2	4

Sample: nine colleges

3.27 When considering FEFC income there are two main scenarios; early mergers and late mergers.

Early mergers

3.28 In those situations where merger took place soon after the establishment of the FE sector, the merged institutions have undoubtedly benefited from substantial growth in funding units. In some cases it is clear that the merged institution achieved growth over and above that which could have been achieved by separate institutions. Thus this level of growth can be directly attributed to the merger. In other situations the level of growth is such that it is impossible to judge whether merger had in fact generated any growth over and above that which would have been achieved by the individual institutions. In either case, it does seem that some of the growth obtained has been at the expense of other FE institutions.

Later mergers

3.29 Those mergers undertaken since 1997 were affected by changes in the policies of the previous government relating to the demand-led element, subsequently reflected in FEFC funding arrangements. Often, these mergers had been planned on the understanding of continuing growth in funding units with consequent improvements in college efficiency. The effect of the changed arrangements has been to inhibit the benefits which can be derived in this way.

Other income sources

3.30 Colleges reported little income growth in other areas of activity which could be directly attributable to merger. Most colleges have ambitions to generate additional external income (income from sources other than the funding councils), and thus reduce their dependence on FEFC income, and were strongly of the view that merger had and would improve their capability to do this as a result of better accommodation and increased academic staff specialisation. Whether merger does actually result in additional external income generation remains to be seen.

3.31 Merger has had little impact on the position of colleges with regard to HE provision. All of the colleges surveyed reported little HE income growth as a consequence of merger, but there was a feeling that perhaps their existing HE income base had been protected.

Curriculum Benefits

3.32 The curriculum benefits achieved through merger are shown in table 5.

Table 5. Curriculum benefits

	<i>Significant</i>	<i>Moderate</i>	<i>Minimal</i>	<i>None</i>
Improved access and progression	4	4	1	—
Development of new curriculum areas	4	4	—	1
Protection of at risk areas	2	4	3	—

Sample: nine colleges

3.33 In those mergers where two colleges from a different group (either general FE, specialist or sixth form college) had come together, the curriculum portfolio before merger had nearly always been incomplete in some respects either in terms of programme area and/or level of provision available. These mergers were seen to provide a comprehensive portfolio of provision at some levels (mainly national vocational qualification (NVQ) levels 1 and 2) with centres of excellence created at NVQ levels 3, 4 and 5 building on the strengths and expertise at each of the founder colleges. Within this model, some rationalisation of provision was possible in duplicate areas — for example, where a specialist college had attempted to diversify its traditional provision into other areas of academic or vocational further education or where a general FE college had expanded its general certificate of education (GCE) A level portfolio in the last few years. Moreover, progression pathways had been created where a level of provision in either founder institution had been missing previously.

3.34 Where two colleges from the same group had merged, the number of groups containing fewer than 10 students had fallen, thus improving the economic viability of the programmes on offer. In some cases however, geographic separation had necessitated the continuation of duplicate provision at each of the merged college sites, at least up to NVQ level 3.

3.35 Pooling of expertise and resources as a result of merger was perceived to provide a platform for future development of new programmes such as in part-time adult, vocational and community provision where none had previously been available in a specific locality, and in higher education, particularly at higher national diploma (HND) level. Joint timetabling between sites in order to provide individual 'mix and match' learning programmes coupled with appropriate transport mechanisms between sites had been developed or expanded in some cases. Modularisation of the entire curriculum had been proposed but not yet implemented in many cases. Modularisation was seen as one means of expanding choice and progression routes and also of improving quality and efficiency in the delivery of key skills development including communications, numeracy and IT literacy.

3.36 Communications mechanisms such as video-conferencing and networking, intended originally to assist course management, were also envisaged as significant developments to support learning and learners in the multi-site environment created by some mergers, although in most cases these had not yet been put in place. However, proposals to develop new learning facilities which had previously been difficult to fund were now beginning to be implemented through the generation of capital receipts or improved borrowing capacity.

3.37 Some physical relocation of areas of provision had occurred or was proposed in the near future, in order to apply facilities and resources available in one or other of the merged colleges to areas of the curriculum which had not previously had access to those resources. Moreover, some relocations had created centres designed to meet the needs of specific client groups, such as adult part-time students, employer-sponsored groups undertaking customised short courses or students with learning difficulties and/or disabilities. Investment in these centres in order to provide appropriate facilities and a conducive learning environment had been seen as a priority and a tangible demonstration of the benefits arising from merger.

3.38 Minority areas of provision had been maintained by, as far as practical, combining small groups in one or other location within the merged institution. No areas of provision previously identified as at risk has been discontinued following merger, but the number of groups providing the same course had sometimes been reduced and fewer contracts had

been generated with external staffing agencies. Dedicated technician support had become available in some curriculum areas through pooling of resources where none had previously been available in one or other merger partner.

3.39 Where links existed with other institutions, before merger, as a means, for example, of delivering part of the curriculum, links with schools, HE or other providers had been maintained and in some cases strengthened as a result of a merger. Similarly, contracts with employers and with local TECs for specific training had been maintained and renewed with the merged institution.

3.40 Harmonisation of recruitment and admission procedures and a similar approach to information and guidance and other learner support systems have provided more effective and efficient services for customers. Students who might previously have enrolled at a small and/or specialist college with limited learner support facilities have been able to access the full range of services and facilities available across the merged institution, particularly where transport arrangements have been made available between sites. Centralisation of specialist teams involved in learner support may have improved the effectiveness of the cross-college operation particularly during busy periods of the year, but has not lead to significant direct savings in staffing costs due to rationalisation of posts. Additional support has been made available to more students than previously in many of the mergers involved in the study and more efficient recording and registering mechanisms have ensured the appropriate claiming of funding units in these areas of activity.

Organisational Benefits

3.41 There are a number of benefits from merger which accrue to the organisation as a whole. These are:

- improved status
- improved resource efficiency
- enhanced managerial practices.

Improved status

3.42 All the colleges in the sample believed that the merger had improved their status in the locality, and had in some cases prevented the encroachment of other colleges into their area. However, some newly merged colleges felt that the change of image and potential temporary loss of identity might cause a downturn in recruitment in the immediate post-merger period. Those who had been merged for over a year reported that they had not experienced any 'downturns' as a direct consequence of merger, possibly because they had mounted extensive marketing campaigns in the lead-up to and at the point of merger to minimise this perceived risk.

3.43 Many colleges also commented that management team energies which had previously been diverted to some of the more time-consuming and potentially wasteful aspects of institutional competition, could now be focused instead on other strategic and developmental priorities.

Improved resource efficiency

3.44 Many colleges cited examples in which merger had led to substantial improvements in the efficiency with which the institution used its resources. To a large extent these

efficiency improvements have come about as a consequence of the growth in student numbers which have been absorbed with few additional resources. Examples include:

- reductions in the numbers of very small class sizes in institutions
- increases in the number of class contact hours of teaching staff bringing them closer to contractual requirements
- more efficient use of buildings
- more efficient use of teaching equipment.

Enhanced managerial practices

3.45 Best practice had been applied to systems and procedures across the merged institutions as a result of the merger, particularly in the areas of financial management and control, data recording and processing and information reporting to support decision-making and to fulfil external stakeholder requirements. Although specialist teams were more likely to exist to perform these functions in large institutions than in small ones, it had not always been the case in the mergers included in the sample, that best practice had been found exclusively in the larger institutions.

3.46 In many cases, the merger had been the catalyst for an institutional reorganisation, and in particular a reconfiguration of the management structure, whether or not a type A or type B (see paragraph 1.2) approach to merger had been adopted. Some savings had been made at senior and middle management levels as a result of such reorganisations, although limited redundancies had resulted. Job evaluation schemes had been used to identify appropriate levels of remuneration for management posts reviewed in the reorganisation process and in some cases where the previous remuneration level had been higher than that proposed in the new structure, convergence over an appropriate period of time had resulted.

3.47 Governing bodies had been reconstituted thus bringing together new combinations of experience and expertise. In many cases, irrespective of the chosen merger type, a joint search committee had been established to appoint governors to the merged college corporation utilising agreed selection criteria. A number of governing bodies had held vacancies open from the time when the merger was first proposed so that combinations of the boards from both merger partners was facilitated without loss of significant numbers of previous board members. It was more likely that equal numbers of board members from each previous corporation would combine to form the new corporation where a type A merger had taken place. In most instances, the chair and vice-chair of each corporation had been invited to become members of the merged corporation to ensure continuity. One college, in which only some of the board members were able to transfer from each of the founder corporations, invited the members who were not selected to attend board meetings for one year following merger in the interests of continuity. In other instances an advisory board related to the specialisms offered by the smaller merger partner in a type B merger was formed from those governors who did not transfer to the board of the merged corporation. The role of clerk to the governors was usually adopted by one of the previous clerks.

■ 4 Costs

Introduction

4.1 The process of merger has significant costs associated with it and when considering merger, these costs have to be set against the actual and prospective benefits described in chapter 3.

4.2 The costs of merger can be described under four main headings:

- staff time
- capital investment
- staff severance
- merger support.

Staff Time

4.3 All the colleges in the survey stressed that in addition to the costs of pre-submission research, feasibility and due diligence exercises, there was a considerable resource input required at all levels, but most significantly management and senior management level. This input was difficult, if not impossible, to quantify and in very few cases had it been recognised by substitution of additional personnel to release staff from their other duties. The additional time commitment had simply been absorbed. Moreover, as vacancies in key posts occurred as a result of normal staff turnover these were often sensibly not filled until the structure of the merged college had been agreed and it was clear that the merger would proceed.

4.4 If care is not taken, such an arrangement could have four serious and deleterious effects:

- it may affect the college's ability to provide data returns, cope with external assessment and inspection concurrent with the merger, or plan in the short-term
- it may affect the college's ability to maintain the quality of its services
- it is likely to produce high levels of stress among senior staff
- it may inhibit the ability of staff to respond to immediate opportunities and unforeseen external requirements and thus detract from college development.

4.5 There are no easy answers to the above problems and all that can be done is to emphasise the need for good forward planning coupled with the provision of temporary and short-term support to managers where necessary. However, some colleges expressed the view that the FEFC submission approval process could be condensed to shorten the merger timescale and reduce the burden on college staff.

Capital Investment

4.6 Institutional merger often results in the need for a significant level of capital investment. Often such investment is made to enable the merged institution to undertake a site rationalisation exercise, as table 6 indicates.

Table 6. Site rationalisation investment

	<i>Significant</i>	<i>Moderate</i>	<i>Minimal</i>	<i>None</i>
Level of capital investment undertaken	1	2	2	4
Future level of capital investment anticipated	7	—	2	—

Sample: nine colleges

4.7 In addition to undertaking capital investment to facilitate site rationalisation, colleges may also undertake capital investment to improve the standard of building stock. Several examples have been quoted of where the pooling of cash resources on merger meant that the richer partner in a merger had financed significant capital investment on the site of the poorer partner for the benefit of all. In one college, such investment amounting to £750,000 was undertaken to improve the quality of teaching accommodation on an under-used site and it is believed that such investment was a key factor in achieving the substantial growth in the number of students attending that site.

4.8 In some cases, capital investment in facilities which would have been undertaken sooner rather than later (for example, IT networks) were held back until after the merger and some colleges felt that they may have fallen behind other colleges in embracing new technology as a result. College reserves and funding earmarked for specific improvements to accommodation (Hunter funds) had not been spent as originally planned because the merger was likely to involve alternative uses for the accommodation earmarked for improvement.

Staff Severance

4.9 In chapter 3 we noted that the academic and support savings resulting from merger were, in most cases, limited. Not surprisingly, therefore, the severance costs associated with such staff savings were also limited as the results in table 7 indicate.

Table 7. Severance costs

	<i>Significant</i>	<i>Moderate</i>	<i>Minimal</i>	<i>None</i>
Severance costs incurred (support staff)	1	2	5	1
Severance costs incurred (teaching staff)	3	2	3	1

Sample: nine colleges

- 4.10 There are, of course a number of key factors which account for this:
- many vacant posts were left unfilled in anticipation of merger
 - the uncertainty caused by merger meant that some staff, who were in posts likely to disappear on merger, left

- some colleges had substantial numbers of staff of retirement age at the time of merger
- the early retirement provisions in force at the time of merger limited the costs falling on colleges (this situation has now changed)
- some staff, who were in posts likely to disappear on merger, had been moved to other posts, sometimes on protected salaries.

Merger Support

4.11 There were two particular areas where external support was felt to be appropriate and where costs had been incurred. Some colleges had commissioned independent research projects on their merger proposals. The costs associated with this exercise were around £40,000 to £60,000 depending on the scale and complexity of the merger proposals. These figures exclude the costs of any management time associated with the exercise. In view of the damage that could be done by pursuing an inappropriate merger, such studies were felt to be worthwhile.

4.12 Before merger, most colleges commissioned some form of due diligence exercise through an external and independent party. The costs of such an exercise were usually of the order of £30,000 to £50,000 depending on the scope and extent. Although such exercises were felt to be essential, some colleges commented on the need to think carefully about the scope and extent of the review to ensure all areas were covered.

■ 5 *Process*

Introduction

5.1 In this chapter we look at the process adopted by institutions to plan and implement mergers. The aim here is to identify examples of good practice and pitfalls to be avoided by those contemplating merger in the future. The issues covered are as follows:

- choosing a merger partner
- merger planning
- project management
- timescale
- resources
- change management and communication.

Choosing a Merger Partner

5.2 In the sample colleges, the choice of partner had come about as a result of one or more of the following factors:

- previous establishment of joint activities and collaborative links so that merger seemed to be the next logical step
- expectations over a number of years that at some time a merger would be achieved, brought forward by a sudden downturn in financial health of one or both of the merger partners
- a realisation that inter-college competition was not improving participation and achievement levels or was damaging the ability of both institutions to achieve their medium- to long-term objectives
- fear of alternative merger possibilities in the locality and sometimes, therefore, the merger being perceived as a defensive counterbalancing strategy
- concern to protect vulnerable minority provision or specialist provision in a locality
- failure of another merger proposal or perception that an opportunity had become available, for example, vacancies occurring for a chief executive or changes in the chair of governors
- the desire to rationalise by mutual agreement rather than by necessity as a result of deterioration in financial health of one or more of the merger partners
- the perception that one particular partner was more desirable than others because that merger would not result in significant rationalisation
- the perception that a merger of all colleges in the locality, while not immediately available, would come about as a result of a merger of two colleges as an interim step

- a joint desire to develop new curriculum areas and levels of provision which would not have been possible in any other partnership combination
- selection of a partner in a sufficiently strong financial position to eliminate debts, ongoing problems and facilitate investment in accommodation and resources. Sometimes a partner was selected to enable the joint estate to be rationalised, thus allowing for capital receipts to be generated.

5.3 The initial approach in the case of colleges of different size, type or financial health had often been made by the 'minority' partner after having conducted an appraisal of its strategic options. In one case, expressions of interest from a number of prospective merger partners had been sought, while in another an initial feasibility study conducted independently had identified the most appropriate combination. Feasibility studies had been conducted in a majority of colleges in the sample but these had tended to be implemented following an initial proposal between two potential partners to verify whether the proposal was sound, rather than before initial selection.

5.4 The question therefore remains as to whether some of the mergers in the study were in fact the right or only combination and whether this should have been confirmed before formal submission of a proposal to the FEFC. Those colleges that had conducted feasibility studies and had identified 'deal breakers' at an early stage had certainly felt confident that once these were overcome the merger was the way forward. They therefore had made rapid progress in planning the steps towards formal submission and harmonisation, and accomplishing their targets within the timescales set.

5.5 Extensive option evaluation and in-depth analysis of all aspects of the position of both merger parties before merger, and as a combined institution in the short-and medium-term, are critical success factors in ensuring that the perceived benefits become reality once the merger has been effected. We suggest that such a review should encompass all aspects of post-16 education in an area and the current and future demands for provision in the light of the existing range of institutions in the area.

Merger Planning

5.6 Effective merger planning is another key success factor in ensuring steady progress and the achievement of merger objectives within the timescales envisaged. An effective plan should incorporate robust feasibility and due diligence studies thus minimising the risk of later problems. Experience has shown that the more wide-ranging and detailed the initial feasibility and due diligence studies had been, the more robust would be the financial and non-financial benefits post-merger. In a number of cases where no initial independent feasibility study had been conducted, the financial projections, on which the success of the merger was predicated, were limited in range and robustness and proved to be inaccurate and over-optimistic. This resulted in more severe rationalisation and greater delays in realising the benefits of merger than had been anticipated.

5.7 Those involved in mergers soon after the establishment of the sector had found planning to be more problematic than those involved more recently, because guidelines for the FEFC had also been evolving in that time period. All the colleges felt that early contact with the FEFC through the regional office, college inspectors and directly with FEFC specialist staff involved nationally with mergers in the sector was essential in order to establish and check procedures and to set 'milestone' dates for various stages of the submission and consultation processes. They had found that visits by FEFC staff to

address joint meetings of the governing bodies or of joint working parties of governors and senior managers had been especially helpful in raising awareness of the procedures of the FEFC and the requirements of the secretary of state.

Project Management

5.8 Best practice among the mergers in the study involved the compilation of detailed project plans which built in the milestones identified throughout the process, allowed slippage time for any unforeseen difficulties, particularly at the early explanatory stages and identified clearly who was responsible for achieving targets and deadlines at each stage of the process. Some colleges advocated that one senior manager should be designated as overall project leader. This was obviously more easily accomplished where it was already clear who would become the chief executive of the merged institution, for example in the case of a type B merger where the chief executive of the corporation ceasing to exist was also intending to retire. However, even in those instances where the issue could not be resolved at the initial planning stage, it had been agreed that project management by committee was undesirable and an individual should be identified to co-ordinate and drive the process forward and to be responsible for providing regular reports to an overall joint steering committee.

5.9 All the colleges in the sample had established joint steering committees to oversee project progress. In most cases this had consisted of the chairs and other senior governors of both merger partners, together with senior managers from both institutions. Formal minutes of the meetings had been kept in many cases and these had provided useful evidence of option appraisal and key decisions when the proposals reached formal consideration by the FEFC regional and reorganisations committees and as background information within consultation documents and internal communication exercises. Generally, some decision-making powers had been delegated from the boards of both the merger partners to the joint working party to allow for rapid progress at some stages of the process and to avoid unnecessary delays due to difficulties in convening frequent board meetings. However, additional time commitments had resulted for governors and in particular for chairs of boards and committees in seeing the process through to conclusion and in communicating with each other, managers and staff.

5.10 Finally, it was emphasised that effective project management was essential to ensure that colleges 'kept their eye on the ball' and did not allow service provision to deteriorate during the merger period. It was stressed that damage to the reputation and image of the college could easily wipe out any benefits which merger could generate.

Timescale

5.11 The general consensus among colleges in the sample was that the merger process should take approximately one year. Some colleges felt that they would have preferred a shorter timescale because the uncertainty and potential damage to staff morale of a long lead-in period was undesirable. Others felt that too short a timescale would put pressure on those managing and steering the project to make decisions without the benefit of all the available management information. This could result in potential risks being overlooked and key issues being only superficially resolved before the formal submission of the proposal to FEFC. Those who had undertaken extensive research at the pre-submission stage certainly felt that this had been worthwhile and had enabled them to progress

smoothly through the later stages of the project because full information had been obtained to respond to consultation feedback and the requirements of the FEFC.

5.12 In identifying an appropriate timescale for merger 'slippage time' had been built into project plans to allow for unforeseen events without creating a significant impact on achievement of targets and deadlines. It was also stressed that project planning related to a number of other key activities, such as the provision of returns to the FEFC and the college's own strategic planning and marketing cycles. These systems also needed to be flexible and adaptable in the light of timescale changes.

Resources

5.13 We have already noted the considerable resource input needed from staff, particularly at management and senior management level, throughout the project period. The extent of this input, particularly among senior management, should not be underestimated and should be planned for accordingly, using temporary and short-term support where necessary.

5.14 Most colleges took the view that it was important to commission a broad-based due diligence review by an external and independent party. Such reviews had identified key issues which might have caused problems further down the line. Beyond that due diligence review, the degree of external support for the merger process commissioned by colleges varied considerably both in scale and type.

Change Management and Communication

5.15 A third key success factor identified by the colleges visited was the need for communication within the institutions involved in the merger. It cannot be stated too strongly that throughout the merger process, senior managers and governors can never spend too much time communicating with staff at all levels. There was a need for clear unambiguous statements by senior management and governors as to what would or would not be happening with regard to a range of issues particularly in relation to security and continuity of employment, conditions of service, line management structures and relocation. Effective communication mechanisms on these issues and others had included staff meetings jointly with members of the merger steering group and senior management teams, regular bulletins, newsletters and briefings. Some colleges had organised the involvement of employees at all levels from both merger partners in joint working groups with a brief to set targets and action plans for the harmonisation of procedures and systems affecting particular areas of work, and to translate curriculum objectives into realistic course proposals and developments. Without these mechanisms it was felt that progress would not have been possible in the timescales envisaged and that at the point of merger, terms and systems would have been dysfunctional and ineffective. The importance of a smooth transition, at the point of merger, both for the customers and the staff of the institutions involved was stressed, in order to ensure that the merger was seen to be of immediate benefit to all concerned.

5.16 It was acknowledged, however, that harmonisation of the culture and structure of both partners could not be achieved rapidly in many cases, particularly where there were fundamental differences in the scale, nature and/or background of the institutions concerned. The communication mechanisms put in place before merger were often

maintained for at least the first 12 months post-merger. Reorganisation of areas of work and of the merged college as a whole occurred frequently within the first 12 months of merger as a result of clarification of structure, roles and responsibilities. Such reorganisations, which did not necessarily always involve rationalisation of provision and services, were seen as useful mechanisms to get the messages across that 'things have changed'. It had also taken time for staff to adopt and to adjust to different working practices. The most effective change management strategies were those where best practice from both merger partners had been adopted rather than where one institution's systems and procedures had been imposed upon the other irrespective of their strengths and weaknesses. In type B mergers, care had been taken to reassure staff from the college no longer in existence as a corporation that their views and requirements would be heard by senior management and taken into account in the organisation and planning processes of the merged institution. In some cases, even three years after merger, it was felt that in some areas of work, divisions still existed and that harmonisation would be an ongoing process for some time to come. Considerable staff development programmes and a high proportion of the staff development budget in the first post-merger year had been allocated to ensure that newly constituted teams within realigned areas of work would perform effectively and corporately within the merged institution.

5.17 In addition to internal communications, many colleges also emphasised the importance of liaising continuously and consulting widely with a wide range of external parties such as: schools, local authorities, members of parliament, TECs, employers and the general public. Furthermore, such external communication should take place in the early stages of the merger process. In its absence it was quite possible for a wide range of misinformation and rumour to be created which could result in major difficulties for colleges which would require yet more senior management time to resolve.

■ 6 *Summary and Conclusions*

Introduction

6.1 We believe that a number of firm conclusions may be drawn from this study . These are described below .

Financial Benefits

6.2 We believe there is strong and compelling evidence that institutional merger has already delivered certain financial benefits in a number of cases and that there will be additional financial benefits generated in future years. This is particularly the case in relation to site rationalisation.

Curriculum Benefits

6.3 All colleges which formed part of this study have been able to identify significant improvements in the range and quality of curriculum offered in the merged institution compared to that which existed previously. It is clear that the curriculum benefits of merger are significantly greater than the financial benefits of merger.

Alternatives to Merger

6.4 The main alternatives to merger are:

- enhanced institutional collaboration
- improvements in the management of existing institutions.

6.5 In some cases (for example, site rationalisations) the financial benefits achieved could almost certainly only have been achieved through merger. In other cases, theoretically, the benefits obtained could have been achieved by other means but, in practice, we are sceptical that this would have been the case. We would pose the question that if such benefits can be achieved in future through enhanced collaboration or improved management, why they have not already been achieved. We have been told on many occasions that it was merger which provided the necessary managerial resources and catalytic effect to facilitate the organisational change which, in turn, produced the benefits referred to earlier.

Maximisation of Benefits

6.6 We have already noted that in some of the mergers that have already taken place, the configuration of the merger (in terms of partners) might not necessarily have been the best available option. Hence, to maximise the benefits of merger it is vital that a full strategic review of post-16 education provision in the area (including school sixth forms and sixth form colleges) is undertaken in advance of a firm decision about merger.

6.7 Furthermore, the benefits of merger are contingent on the specific circumstances of the individual merger partners and no firm generalisations about merger benefits can be made. Thus before a firm decision about merger is made it is vital to undertake a full evaluation of the likely benefits.

Merger Workload

6.8 It cannot be over-emphasised that institutional merger is a complex and time-consuming process. The burden on staff and governors in the institutions is immense. Neither can it be assumed that this workload burden will disappear once merger has taken place since there are almost certain to be ongoing issues which will take many years to resolve.

